



**THE INSTITUTE
OF CHARTERED
ACCOUNTANTS**
IN ENGLAND AND WALES

ICAEW TAX FACULTY REPRESENTATION

TAXREP 12/11

DRAFT FINANCE BILL 2011: EMPLOYER SUPPORTED CHILDCARE

Comments submitted on 9 February 2011 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales on the proposed legislation on 'Employer supported childcare: changes to tax relief' published as part of the draft Finance Bill 2011 on 9 December 2010.

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INTRODUCTION

1. This document sets out the comments of the Tax Faculty of the Institute of Chartered Accountants in England and Wales (ICAEW) on the proposed legislation on **Employer supported childcare: changes to tax relief** published as part of the draft Finance Bill 2011 on 9 December 2010.
2. These comments were sent to the HMRC officer responsible for this topic on 9 February 2011.
3. They are also included in our comprehensive response to the draft Finance Bill 2011, which is published as TAXREP 5/11 and was submitted to the Exchequer Secretary to the Treasury and to the Permanent Secretary for Tax at HMRC on 9 February 2011.
4. Information about the Tax Faculty and the ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's ten tenets for a better tax system, by which we benchmark proposals to change the tax system.

WHO WE ARE

5. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 775,000 members worldwide.
6. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
7. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter *TAXline* to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire.

KEY POINTS

8. We are concerned that the way in which it is proposed to restrict employer supported childcare to the basic rate, through the PAYE system, will prove not to be practicable and will create very considerable burdens for business. We recommended in our paper submitted in March 2010 that the policy objective would be best achieved by requiring employers to return the excess benefit on forms P11D so that the benefit-in-kind is processed by HMRC in exactly the same way as any other benefit-in-kind.
9. We urge the Government to reconsider the mechanism by which the policy objective is to be achieved.

COMMENTS ON THE DRAFT PROVISIONS

10. From April 2011 employer supported childcare (ESC) will be restricted to the basic rate. We are concerned about the practicality of this proposal. In order to restrict the relief, employers will be required to estimate the marginal tax rates of their employees. Previous experience in a related area, namely seeking to limit the benefit of married persons' allowance to the basic rate, was abandoned because it was impractical to implement this via the PAYE system.
11. We commented on 22 March 2010 (published as TAXREP 20/10) on HMRC's Technical Note published on 19 February 2010. At that time we recommended that employers simply return the excess benefit on forms P11D so that the benefit-in-kind is processed by HMRC in exactly the same way as any other benefit-in-kind. We still consider that that would be the least burdensome approach and in practical terms is likely to be the only sensible way of achieving the desired policy objective of limiting tax relief to basic rate.
12. We welcome the fact that the burden on employers has been reduced in the draft legislation published on 9 December because employers will no longer be expected to both undertake an estimate and complete forms P11D. But employers will still have to make the estimate which will be burdensome and open to error, manipulation and abuse, and in the case of employees whose other income takes them into a marginal rate of tax which is higher than that applied to the earnings of the employment in which the ESC is provided, the employer estimates will give an answer which is at variance with the policy objective of giving less relief to those whose marginal tax rates are above basic rate.
13. In addition, the number of different types of income that have to be included will involve the payroll department having to undertake a number of time consuming and burdensome calculations. Furthermore, it is not clear the extent to which bonuses, which may not have been fixed, should be taken into account, or even confidential future plans that are being considered for execution in the forthcoming tax year, for example, to close a division, and which will impact on the affected employees' taxable pay. We should welcome confirmation that in cases such as this the previous year's income can be taken as a reasonable estimate.
14. We note the attempt to make the estimates more accurate by requiring the adjustment for 'coded-in personal allowances' but, as defined in new section 318AA (4), this is a figure which it is impossible for any employer to ascertain without involving his employee because the coding notifications provided to employers by HMRC consist of an overall figure – or may even be a K code or a code which does not cite a figure, like BR or OT. Having to obtain information from employees will increase the time and hence the cost of compliance.
15. If the estimate process is to be retained, with all the inherent risks of a breakdown in employer/employee relations, we recommend that the personal allowance that is applied should be based on the estimated income on the assumption that that income is total income for the year so that the employers do not have to refer elsewhere.
16. We should also welcome clarification, preferably by way of a ministerial statement, of the steps that employers will have to take to satisfy HMRC (eg in a PAYE compliance audit) and employees (eg who object to the estimated rate of tax arrived at by the employer) that they have done all that is necessary – ie taken reasonable care – to comply with the law in making the estimate, and whether penalties for an incorrect end of year return P35 will arise owing to an estimate that is found to be wrong.

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APPENDIX 1

THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99.